

Marginal Properties Workshop Minutes
January 23, 1997

1. Reviewed action items from 10/31/96 marginal properties workshop

a. Debbie Gibbs-Tschudy reported that MMS' solicitor stated that interest would not be payable to the states merely because payment relief is granted for a marginal property under Section 7. Interest is payable to a state when

- 1) MMS collects monies but fails to disburse the state's share of those monies within the prescribed time frames or**
- 2) MMS collects a late payment charge which is sharable with the state.**

b. Patsy Bragg and Mike Deberard provided summaries of Federal and state incentive program requirements for participants, relevant portions of which are attached to these minutes.

c. Nick Fadely reported that Tammy Naron had several meetings with offshore production personnel from Apache. Tammy indicated that Apache looked at defining offshore marginal properties from both production and dollar levels. For production-based levels, Apache found that while some well's production might not be individually economic, others having similar production levels could be economic if in proximity to other wells that secure favorable transportation rates. Therefore Apache concluded marginal production levels would be difficult to quantify. For dollar-based levels, Apache concluded that "marginal" depends on the interest owners. Some have costs better under control than others. Company overhead and G&A costs vary greatly, so establishing marginal dollar levels would also be difficult.

Tammy concluded that lessees may need to submit specific financial justification to seek relief for their marginal OCS properties.

d. Mike Deberard reported that DOE does not have any prepayment (or similar discounting) programs for the Naval Petroleum Reserve that MMS could use as a model.

e. Dave Domagala reported that MMS had reviewed DOE's Agency Information Agency price forecasting reports and that they appeared to use standard economic projection techniques.

f. Debbie Gibbs-Tschudy indicated that MMS' state delegation team was determining the appropriate state officials that would be responsible for reviewing and approving prepayment and relief applications for marginal properties under RSFA Section 7.

2. The participants reviewed the state incentive program levels to determine their potential for use in submitting applications under Section 7. The participants generally decided that using them would be difficult for both industry and MMS.

The group then discussed using the 15 bbl / 90 mcf levels in Section 6(d)(4) of RSFA (exception to entitlement reporting for marginal properties) for marginal properties under Section 7. Most believed these would be reasonable levels to submit an application for onshore marginal properties. Ben Dillon offered to use IPAA's offshore marginal property

workgroup to assist in determining offshore marginal property levels. Ben offered to allow major companies and MMS to participate in this effort. Concern was expressed by MMS and state representatives that the 15/90 level might result in too many onshore applications. Wanda Fleming stated that 80-90 percent of Montana properties might qualify as marginal at these levels.

The participants also generally agreed that the marginal property definition was not intended to include small working interests in a property of sizable production - the definition was intended to cover only a small producing property.

3. MMS' draft regulation outline for accounting and auditing relief was reviewed. Because of the time frames involved, the remainder of the workshop was focused primarily on the accounting and auditing relief portion of Section 7. A future workshop will be scheduled to cover the prepayment portion of Section 7.

Discussion focused on the various forms of accounting and auditing relief that would be made available. The following possible types of relief were discussed:

- a. Measurement relief: semi-annual actual gas measurement with allocated volumes used for monthly production reporting
- b. Net-entry adjustments: one-line adjustment reporting on Form MMS-2014
- c. Rolled-up royalty reporting: multiple months, multiple leases, or multiple selling arrangements
- d. Delayed reporting: semi-annual or annual reporting (pay at end, middle, or beginning of period)
- e. Threshold volumes or dollar amounts requiring little reporting (use for smallest of marginal properties only)
- f. Form MMS-2014 EZ: simplified reporting with less data required
- g. Audit relief: reduced audits
- h. Royalty in-kind: royalty obligation satisfied by government taking marginal production in kind
- i. Alternate valuation: simplified valuation with fixed and certain basis
- j. Waiver of de minimus royalty or interest (use for smallest of marginal properties only)

Discussion also centered around application process. Many felt that some relief could be granted using a notification process instead of a specific application that required approval. It was agreed that if the MMS and states could agree on specific conditions allowing notification only, they would be provided for in the agency-issued guidelines, not in the regulation. In addition, Wanda Fleming suggested an application processing fee might be necessary. Generally, many expressed that an application fee would prevent many, if not most, eligible marginal property owners from seeking relief. In addition, the topic of appeal rights for a denied application was discussed. MMS will check with the solicitor's office to determine the requirements for appeals based on application denials.

4. A discussion of pilots for marginal properties was held after many participants had left. MMS plans to send a Dear Payor Letter to all current oil and gas payors to solicit interest in volunteering for a pilot. It was discussed that several actual, accounting and auditing

relief pilots could be conducted now, but any prepayment pilots are restricted by RSFA, i.e., MMS can not accept a prepayment until at least 2 years from enactment of RSFA. Therefore, a prepayment pilot would have to involve the application and negotiation phases of the process only.

MMS is targeting the Dear Payor Letter to be issued in early March and the pilots to begin in early April 1997.